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Reorganizations, Mergers or
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REORGANIZATIONS, MERGERS, OR 4± CONSOLIDATIONS

Excerpts from the Federal Revenue Act of
1918, bearing on the subject, together
with department regulations
and rulings

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[The data herein contained
is official to March 15, 1921.]

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THE
CORPORATION TRUST COMPANY

37 WALL STREET, NEW YORK

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C8227X

Foreword

As a ready reference for the use of attorneys when considering reorganizations, mergers, or consolidations, we have prepared this pamphlet containing all of the official matter issued to March 15, 1921.

We do not, in this pamphlet, express any conclusions of our own, but merely have collected the departmental rulings and regulations.

Before any final conclusions are arrived at, care should be taken to see that none of the rulings herein contained has been amended or superseded.

We welcome the opportunity of assisting members of the bar in corporation matters and shall be glad to have any lawyer take up with us questions concerning the organization or reorganization of a company. We are prepared to furnish information as to the requirements of all of the states, as well as to advise members of the bar of any rulings of the Treasury Department promulgated since the issuance of this pamphlet.

THE CORPORATION TRUST COMPANY.

March 15, 1921.

GJS

[The data herein contained is official to March 15, 1921.]

Reorganizations, Mergers, or Consolidations

(*Revenue Act of 1918.*)

PART II.—INCOME TAX.

Basis for Determining Gain or Loss.

Sec. 202 (a) * * * *

(b) When property is exchanged for other property, the property received in exchange shall for the purpose of determining gain or loss be treated as the equivalent of cash to the amount of its fair market value, if any;

but when in connection with the reorganization, merger, or consolidation of a corporation a person receives in place of stock or securities owned by him new stock or securities of no greater aggregate par or face value,

no gain or loss shall be deemed to occur from the exchange, and the new stock or securities received shall be treated as taking the place of the stock, securities, or property exchanged.

When in the case of any such reorganization, merger or consolidation the aggregate par or face value of the new stock or securities received is in excess of the aggregate par or face value of the stock or securities exchanged, a like amount in par or face value of the new stock or securities received shall be treated as taking the place of the stock or securities exchanged, and the amount of the excess in par or face value shall be treated as a gain to the extent that the fair market value of the new stock or securities is greater than the cost (or if acquired prior to March 1, 1913, the fair market value as of that date) of the stock or securities exchanged.

Regulations No. 45, Revised to March 15, 1921, and available special rulings.

Exchange of Stock for Other Stock of no Greater Par Value.—

In general, where two (or more) corporations unite their properties, by either (a) the dissolution of corporation B and the sale of its assets to corporation A, or (b) the sale of its property by B to A and the dissolution of B, or (c) the sale of the stock of B to A and the dissolution of B, or (d) the merger of B into A, or (e) the consolidation of the corporations, no taxable income is received from the transaction by A or B or the stockholders of either, provide

REORGANIZATIONS, MERGERS

the sole consideration received by B and its stockholders in (a), (b), (c), and (d) is stock or securities of A, and by A and B and their stockholders in (e) is stock or securities of the consolidated corporation, in any case of no greater aggregate par or face value than the old stock and securities surrendered. The term 'reorganization', as used in Section 202 of the statute, includes cases of corporate readjustment where stockholders exchange their stock for the stock of a holding corporation, provided the holding corporation and the original corporation, in which it holds stock, are so closely related that the two corporations are affiliated as defined in Section 240 (b) of the statute and article 633, and are thus required to file consolidated returns. So-called 'no-par-value stock' issued under a statute or statutes which require the corporation to fix in a certificate or on its books of account or otherwise an amount of capital or an amount of stock issued which may not be impaired by the distribution of dividends, will for the purpose of this section be deemed to have a par value representing an aliquot part of such amount, proper account being taken of any preferred stock issued with a preference as to principal. In the case (if any) in which no such amount of capital or issued stock is so required, 'no-par-value stock' received in exchange will be regarded for purposes of this section as having in fact no par or face value, and consequently as having 'no greater aggregate or face value' than the stock or securities exchanged therefor. (Art. 1567 of Reg. 45, Rev., January 28, 1921.)

Application of the Limitation as to "No Greater Aggregate Par or Face Value."—In interpreting Article 1567, as amended, the opinion has been expressed that the phrase "in any case of no greater aggregate par or face value than the old stock and securities surrendered" is a limitation governing only "(e) the consolidation of the corporations," and not a limitation with respect to (a), (b), (c) and (d). The statute indicates that the limitation intended by the Regulations is applicable to (a), (b), (c), (d) and (e). (Answer.) You also ask whether in interpreting Article 1567 of Regulations No. 45, as amended, the phrase "in any case of no greater aggregate par or face value than the old stock and securities surrendered" is a limitation governing only "(e) the consolidation of the corporation," or a limitation applying to each of the subdivisions (a), (b), (c), (d) and (e). ¶In reply you are advised that this phrase limits not only subdivision (e), but also the preceding subdivisions. This article of the regulations is founded on Section 202 (b) of the Revenue Act of 1918, which would afford no basis for attaching this qualification to subdivision (e) only. (Letter, embodying inquiries, from Baker and Baker, Washington, D. C., and the letter of reply signed by Commissioner Daniel C. Roper, and dated October 16, 1919.)

Determination of Gain or Loss from Subsequent Sale.—The new stock and securities received as described in the preceding Article [Art. 1567] take the place of the old stock and securities. For the

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OR CONSOLIDATIONS

purpose, therefore, of ascertaining the gain derived or loss sustained from the subsequent sale of any stock of A or of the consolidated corporation, so received, the original cost to the taxpayer or the fair market value as of March 1, 1913, of the stock of B or A in respect of which the new stock was issued, less any untaxed distribution made to the taxpayer by A out of the former capital or surplus of B, or by the consolidated corporation out of the former capital or surplus of A or B, is the basis for determining the amount of such gain or loss. When securities of a single class are exchanged for new securities of the same total par value but of different classes for purposes of determining profit or loss on subsequent sale of any of the new securities, the proportion of original cost (or value as of March 1, 1913) to be allocated to each class of new securities is that proportion which the market value of the particular class bears to the market value of all securities received on the date of the exchange. For example, if 100 shares of common stock, par value \$100, are exchanged for 50 shares of preferred and 50 shares of common each of \$100 par value, and the cost of the old stock was \$250 per share, or \$25,000, but the market value of the preferred on the date of exchange was \$110 per share, or \$5,500 for the 50 shares, and the market value of the common was \$440 per share, or \$22,000 for the 50 shares of common, one-fifth of the original cost, or \$5,000, would be regarded as the cost of the preferred and four-fifths, or \$20,000, as the cost of the common. Similarly, the cost after reorganization, merger, or consolidation of the assets of A or of the consolidated corporation is the sum of the cost (or the fair market value as of March 1, 1913) of the assets of A and of B for the purpose of ascertaining the gain or loss upon a subsequent sale. The new invested capital of A or of the consolidated corporation is to be determined as if A and B were rendering a consolidated return as affiliated corporations. See sections 240 and 326 of the statute and articles 631-638 and 864-869. (Art. 1568 of Reg. 45, Rev., January 28, 1921.)

Exchange of Stock for Other Stock of Greater Par Value.—If in the case of any reorganization, merger, or consolidation the aggregate par or face value of the new stock or securities received is in excess of the aggregate par or face value of the stock and securities exchanged, income will be realized from the transaction by the recipients of the new stock or securities to an amount limited by (a) the excess of the par or face value of the new stock or securities over the par or face value of the old and (b) the excess of the fair market value of the new stock or securities over the cost or fair market value as of March 1, 1913, of the old. In other words, the taxable profit will be (a) or (b), whichever is less. Upon a subsequent sale of the new stock or securities their cost to the taxpayer will be the cost or fair market value as of March 1, 1913, of the old stock and securities, plus the profit taxed on the exchange. (Art. 1569, Reg. 45, Rev., January 28, 1921.)

REORGANIZATIONS; MERGERS

Art. 1563. Exchange of Property [Inserted here for the purpose of showing the definition of "market value."]—Gain or loss arising from the acquisition and subsequent disposition of property is realized when as the result of a transaction between the owner and another person the property is converted into cash or into property (a) that is essentially different from the property disposed of, and (b) that has a market value. In other words, both (a) a change in substance and not merely in form, and (b) a change into the equivalent of cash, are required to complete or close a transaction from which income may be realized. By way of illustration, if a man owning ten shares of listed stock exchanges his stock certificate for a voting trust certificate, no income is realized, because the conversion is merely in form; or if he exchanges his stock for stock in a small, closely held corporation, no income is realized if the new stock has no market value, although the conversion is more than formal; but if he exchanges his stock for a liberty bond, income may be realized, because the conversion is into independent property having a market value. "Market value" is the price at which a seller willing to sell at a fair price and a buyer willing to buy at a fair price, both having reasonable knowledge of the facts, will trade. Property received in exchange for other property has no "fair market value" for the purpose of determining gain or loss resulting from such exchange when, owing to the condition of the market, there can be no reasonable expectation that the owner of the property, though wishing to sell and any person wishing to buy will agree upon a price at which to trade unless one or the other is under some peculiar compulsion. It does not follow that property has no "fair market value" merely because there is no price therefor established by public sales or sales in the way of ordinary business. The property received in exchange may be real estate, personal property, or a chose in action. Where the owner of a bond exercises the right, provided for in the bond, of converting the bond into stock in the obligor corporation, such transaction does not result in a realization of profit or loss, the transaction not being closed for purposes of income taxation until such stock is sold. (Art. 1563 of Reg. 45, Rev., January 28, 1921.)

(The following is a digest of a ruling from Bulletin No. 45 of the 1920 Series of Departmental Bulletin Rulings.)

Section 202, Article 1567: Exchange of stock for other stock of no greater par value.

Where two existing corporations are consolidated under the Act of the General Assembly of Ohio, approved May 29, 1919, by the exchange of no-par-value shares of the new corporation for the entire assets and obligations of each of the existing corporations, the shares of no-par-value stock of the consolidated corporation will be deemed, for Federal income tax purposes, to have a par value repre-

OR CONSOLIDATIONS

senting an aliquot part of the amount of capital with which the corporation is to carry on business as stated in its articles of incorporation.

If the net value of the assets of the corporations which were consolidated exceeds the amount of capital specified in the articles of incorporation of the new corporation, such excess will constitute paid-in surplus out of which dividends might be paid. (45-20-1286: Sol. Op. 72.)

(The three rulings following are from the 1919 Cumulative Bulletin of Departmental Rulings.)

Section 202, Article 1567: Exchange of stock for other stock of no greater par value.

Revenue Act of 1918, Section 202.

1. Mere multiplication of the number of shares of a corporation (resulting from the exchange of four new shares, each having a par value of \$25 for each old share of \$100 par value) when not accompanied by conversion of surplus into capital stock or revaluation of assets, does not give rise to taxable gain or income to stockholders making the exchange.

2. Where a corporation amends its charter so that instead of having 10,000 shares of no-par value, the same stockholders will hold 100,000 shares without par value, neither the original charter nor the amendment having any stated capital in dollars, this multiplication of shares being not accompanied by conversion of assets into capital stock or any revaluation of assets, such a transaction does not give rise to taxable gain or income to stockholders making the exchange.

(A) A corporation, having an authorized and issued capital stock each share of which has a par value of 4x dollars, proposes, after appropriate amendment of its charter, in effect to divide such capital stock by reducing the par value of each share to x dollars per share, and by exchanging with each stockholder four new shares for one old share. Will the new shares constitute taxable income in the hands of the stockholders; and if so, to what extent?

(B) A corporation, having an authorized and issued capital stock represented by shares of no-par value, but having no stated capital in dollars, proposes, after appropriate amendment of its charter, to have such capital stock represented by an increased number of shares without par value, the new shares to be exchanged for the old on a basis of 10 to 1. No transfer of surplus to capital will be made in connection with the transaction. Will the new shares constitute taxable income in the hands of the stockholders; and if so, to what extent?

The corporation mentioned in paragraph (B) of the attached letter has been in existence for several years and is a going concern. No

REORGANIZATIONS, MERGERS

revaluation of its assets is contemplated in connection with the proposed transaction, and its surplus will be exactly the same after as before the issuance of the new shares. The object which is sought to be accomplished in cases (A) and (B) is identical; namely, to reduce the market value of each share of the corporations involved and to thus increase the marketability of all the shares.

The new shares will not constitute taxable income in the hands of the stockholders, or more accurately stated, neither transaction will give rise to gain, profit, or income taxable to the stockholders concerned. (12-19-396: T. B. R. 39.)

Section 202, Article 1567: Exchange of stock for other stock of no greater par value.

For the purpose of determining whether any taxable income is derived by each individual stockholder of a corporation from such transactions as described in article 1567 of Regulations 45, the phrase "aggregate par value" as used in that article means the aggregate par value of stock of each individual stockholder exchanged for new stock and the aggregate par value of such new stock received by each individual stockholder. (10-19-353: O. D. 204.)

Section 202, Article 1568: Determination of gain or loss from subsequent sale.

The word "or" as used in the phrase "stock or securities" in section 202 (b) of the Revenue Act of 1918 is synonymous with the word "and," and when taken in connection with that section means that in case of a reorganization, merger, or consolidation of a corporation, a person may turn in either stock or securities, or both, and accept in exchange therefor either new stock or securities, or both, of no greater par or face value, without being liable for tax on any gain from such exchange. (29-19-623: O. D. 335.)

(The following ruling is from Bulletin No. 20 of the 1920 Series of Departmental Bulletin Rulings.)

Section 202, Article 1568: Determination of gain or loss from subsequent sale.

Revenue Act of 1917.

In re: The appeal of A from the action of the Unit in holding that profit was realized by him upon the sale of certain railroad stock which he owned.

The Committee has had under consideration the appeal of A from a ruling of the Income Tax Unit holding that profit was realized by the taxpayer upon the sale of certain railroad stock owned by him.

The facts appear to be that the taxpayer individually built and

OR CONSOLIDATIONS

owned a railroad which was constructed for the sole purpose of carrying the product of the taxpayer's mills to stations on other roads for distribution. The State Railroad Commission required the incorporation of this road, which was done in 1914. The appraised value of the property as of March 1, 1913, was 30x dollars, the cost of additions between that date and the date of incorporation being 12x dollars, making a total of 42x dollars. Against this amount bonds were issued to the amount of 20x dollars, the total proceeds being received by A, reducing his investment on the above basis to 22x dollars. Against this the Commission permitted the issuance of stock in the amount of 30x dollars. The taxpayer now contends that at the time of incorporation the property was worth the 30x dollars for which it was incorporated, and that profit, if any, was made in 1914 at the time of incorporation and a loss suffered when the stock of the railroad was sold in 1917 for 27x dollars.

The Unit has ignored the possibility of accretion in value of these assets between March 1, 1913, and the date of incorporation. Whatever accretion there may have been in these values would clearly, under the rulings of the office, be taxable profit when converted into stock of the corporation, since the stock would be deemed to be at least equal in value to the assets behind it.

It is further contended by the taxpayer that under numerous decisions of the office where property is exchanged for stock the stock will be deemed to be worth its par value in the absence of evidence to the contrary. Had there been no appraisal of the property, the Committee is of the opinion that this position would have been well taken and that the burden of proof would have been on the Government to show that the stock was worth less than its par value had the taxpayer claimed it to be of value equal to or greater than par. However, the appraisal about that time appears to establish that the property turned over to the corporation was worth less than the par value of the stock received. Undoubtedly that appraisal would have been recognized by the Unit in 1914 as establishing the fact that no profit was then realized by the taxpayer had he presented such claim during that year.

The Committee is therefore of the opinion that in the absence of evidence conclusively proving that at the time the property was turned over to the corporation in 1914 it was of greater value than indicated by the appraisal as of March 1, 1913, no profit can be deemed to have been made in 1914, and consequently that the difference between the value of the stock at that time so determined and the sale price of 1917 is taxable profit in the latter year. (22-20-967: A. R. R. 126.)

REORGANIZATIONS, MERGERS

(*Revenue Act of 1918.*)

PART III.—WAR-PROFITS AND EXCESS-PROFITS TAX

Reorganizations after March 3, 1917. Sec. 331. In the case of the reorganization, consolidation, or change of ownership of a trade or business, or change of ownership of property, after March 3, 1917, if an interest or control in such trade or business or property of 50 per centum or more remains in the same persons, or any of them, then no asset transferred or received from the previous owner shall, for the purpose of determining invested capital, be allowed a greater value than would have been allowed under this title in computing the invested capital of such previous owner if such asset had not been so transferred or received: Provided, That if such previous owner was not a corporation, then the value of any asset so transferred or received shall be taken at its cost of acquisition (at the date when acquired by such previous owner) with proper allowance for depreciation, impairment, betterment or development, but no addition to the original cost shall be made for any charge or expenditure deducted as expense or otherwise on or after March 1, 1913, in computing the net income of such previous owner for purposes of taxation.

(*Regulations No. 45, Revised to March 15, 1921.*)

Valuation of Assets upon Reorganization.

Art. 941. Valuation of Asset upon Change of Ownership.—Where a business is reorganized, consolidated or transferred, or property is transferred, after March 3, 1917, and an interest or control of fifty per cent or greater in such business or property remains in any of the previous owners, then for the purpose of determining invested capital each asset so transferred is valued (a) as if still in the possession of the previous owner, if a corporation, or, if not a corporation, (b) at its cost to such previous owner, with proper adjustments for losses and improvements. This provision is accordingly concerned with the computation of invested capital for the taxable year, while section 330 of the statute is chiefly concerned with the determination of invested capital for the prewar period. See articles 931, 932 and 1561-1570. (Art. 941, Reg. 45, Rev., Jan. 28, 1921.)

(*The following ruling is from Bulletin No. 3 of the 1920 Series of Departmental Bulletin Rulings.*)

Section 331, Article 941: Valuation of asset upon change of ownership.

Mere change of domicile without change as to capital and surplus held not to affect the invested capital, which remains the same for the new company as for the old.

The facts in the case appear to be that the M Company, a cor-

OR CONSOLIDATIONS

poration organized in a certain State, decided that its development would be hampered by its organization in that State and it was therefore decided to reincorporate the company in another State. Accordingly, a new corporation was formed in another State which exchanged its stock directly with the stockholders of the old corporation for their stock, share for share. No change was made in the capitalization or the surplus, but after it had acquired all of the stock of the old corporation the assets of the old corporation were transferred to the new corporation and the charter of the old corporation surrendered. This was in essence merely a reincorporation in a different State without essential change as to business, capitalization, or surplus.

The change of domicile took place in 1916, and the Committee has considered a number of precedents established under the acts of 1913 and 1916 with regard to the treatment of essentially similar transactions. It finds that under such conditions it was the practice of the Bureau to require only one return as covering the income of both the old and the new corporation. It also finds that in numerous cases it was held that no income accrued to the stockholders by reason of exchange of their stock in the old for stock in the new corporation.

The Committee is of the opinion that it is not necessary to make any radical departure from the "distinct entity" theory which has been the guide of the bureau in the past, but feels that where there is merely a transfer of domicile through the surrender of the charter issued in one State and the taking out of a new charter in another State, without any change in the business or amount of the capital and surplus of the corporation, that the new company is entitled to the same invested capital as the old.

It is therefore recommended that the M Company (new) be permitted to use the invested capital which would have been permitted the M Company (old) if there had been no surrender of charter, and change of domicile.

(The following ruling is from Bulletin No. 15 of the 1920 Series of Departmental Bulletin Rulings.)

Section 331, Article 941: Valuation of asset upon change of ownership.

The provisions of section 331 of the Revenue Act of 1918 relate only to the computation of invested capital. In the reorganization of a corporation owning timber lands and engaging in the manufacture of lumber, the basis for deductions for depletion of the timber and depreciation of the plant, machinery and patents claimed by the reorganized company is the cost of these assets at the time they were acquired in reorganization, or their fair market value as of March 1, 1913, if acquired prior thereto.

REORGANIZATIONS, MERGERS

(The following ruling is from Bulletin No. 42 of the 1920 Series of Departmental Bulletin Rulings.)

Section 331, Article 941: Valuation of asset upon change of ownership.

The Committee has had under consideration the appeal of the M Company, from the action of the Income Tax Unit eliminating an item of 40x dollars from the invested capital claimed for the years 1917 and 1918.

It appears that the N Company, a Massachusetts corporation, was organized in 1907; that in 1917 the M Company was organized under the laws of the State of Connecticut, with an authorized capital stock of 150x dollars, of which 80x dollars was issued for the purpose of taking over all the assets and liabilities of the N Company, a Massachusetts corporation. The charter of the reorganized corporation was drafted so that the corporation could engage in the collateral business of owning and renting real estate in addition to its regular business.

In 1917, subsequent to March 3, the newly organized corporation took over the entire assets and assumed the liabilities of the Massachusetts corporation. Some time after that date the Massachusetts corporation surrendered its charter and was dissolved.

A complete field audit of the returns filed by the M Company for the years 1917 and 1918, has been made and the report has been received, audited, and accepted by the Income Tax Unit. Minor adjustments were made in the net income for these years, all of which have apparently been accepted by the corporation. The additional tax found is due largely to the adjustment of the invested capital for these years.

The revenue agent in his report deals quite fully with the reorganization of the corporation and the transfer to it of certain parcels of improved real estate by A, the principal stockholder of both corporations. It appears that soon after the transfer of the assets of the Massachusetts corporation to the M Company, the newly organized corporation, A, its principal stockholder, transferred certain real estate to the new corporation for stock. Such transfer was made after March 3, 1917, and the revenue agent has included in invested capital for both years the adjusted cost of such real estate to A.

The adjustment made was proper for 1918, and was in accordance with the provisions of section 331 of the Revenue Act of 1918, and article 941 of Regulations 45. The same adjustment for 1917 was not proper if the corporation can show that at the time of acquisition of the real estate in question such real estate had a cash value in excess of the adjusted cost allowed by the revenue agent.

It will be noted that in section 208 of the Revenue Act of 1917 the phrase "or change of ownership of property after March 3, 1917," does not appear, but section 208 deals with reorganizations, consolidations, or change of ownership of a trade or business after March 3,

OR CONSOLIDATIONS

1917, where 50 per cent of the control remains with the same person or persons, Section 331 of the Revenue Act of 1918 goes a little further and takes in any change of ownership of property after March 3, 1917, where an interest or control in such trade or business or property of 50 per cent or more remains in the same person or persons. In accordance with the above and under the provisions of section 208 of the Revenue Act of 1917, if the corporation can show that the real estate acquired from A after March 3, 1917, even though 50 per cent or more of the ownership remains in A, had a value in excess of the cost as adjusted by the revenue agent, the corporation is entitled to include the actual cash value of the property at the date of acquisition. This is not true, however, with respect to the 1918 return. The limitation is extended by the provisions of section 331 to any change of ownership of property after March 3, 1917, where an interest or control of 50 per cent or more remains in the same person or persons. The amount which can be included in the computation of invested capital is limited to the actual cost, plus improvements, less depreciation, of the physical property so transferred. Therefore the adjustment made by the revenue agent for 1918 appears to be proper, and his action in reducing the invested capital to the adjusted cost of the real estate in question is sustained. An examination of the record does not show that satisfactory evidence has been submitted by the corporation establishing the value of the real estate transferred to the new corporation in 1917 in excess of the adjusted cost. Therefore it is recommended that the adjustment made by the revenue agent and accepted by the Unit be affirmed.

In the examination of this case the revenue agent has apparently erred by treating the return filed by the corporation under the first two sentences of article 206 of Regulations 33, revised, which reads as follows:

A mere change in name does not constitute a new corporation. If the business was continuous throughout the year, no change in management or operation other than the change in name having occurred, the return should be made covering the business transacted throughout the year, such return to be made by the corporation in the name which it bears at the end of the year, with a notation on the return to the effect that the name had been changed, giving both the old and the new names. If, however, a distinctly new corporation was organized to take over the property of the old, both corporations will be required to make separate returns covering the periods of the year during which they were respectively in charge of the business.

It appears that a new corporation was created to take over the assets of the old corporation, that the authorized capital stock was increased, and that by the new charter the new corporation was authorized to hold title to real estate. A distinctly new corporation came into existence, which took over the property of the old corporation; therefore, both the old and the new corporations will be required to file separate returns covering the periods of the year during which they were in active control of the business. The last sentence of the above-quoted article of the regulations in the judg-

REORGANIZATIONS, MERGERS

ment of the Committee covers the situation in the instant case. Therefore it is recommended that the action of the Income Tax Unit accepting the revenue agent's recommendation on this point be reversed and that both the old and the new corporations be required to render separate returns for the respective periods of the year. It is also suggested that the net earnings, if any, of the Massachusetts corporation from January 1 to the date of dissolution be included as part of the invested capital of the newly organized corporation for the period for which a return is rendered. (42-20-1252: A. R. R. 285.)

(The following ruling is from Bulletin No. 5 of the 1921 Series of Departmental Bulletin Rulings.)

Section 331, Article 941: Valuation of asset upon change of ownership.

The M Company was incorporated for the purpose of acquiring that part of the business of the N Company, a foreign corporation, which it carried on in the United States and Canada.

The M Company issued common and preferred stock to the N Company, in the amount of x dollars, in exchange for its business in the United States and Canada. The domestic corporation requested permission to set up on its books as invested capital several increases over the amounts carried on its books for the same items by the foreign corporation.

Held, that where a foreign corporation has been taxed on its activities in this country, and its activities in Canada and this country are subsequently taken over by a domestic corporation organized for that purpose, and fifty per centum or more of the stock of the domestic corporation is held by the foreign corporation, the assets of the domestic corporation are to be valued under section 331, Revenue Act of 1918. In the case presented the domestic corporation may set up on its books as invested capital the assets taken over from the foreign corporation at such values as could have been established had the previous owner been required to set up invested capital as a domestic corporation. (5-21-1424: O. D. 789.)

(Revenue Act of 1918.)

TITLE XI.—STAMP TAXES.

SCHEDULE A.—Stamp Taxes.

1. Bonds of indebtedness . * * * *
2. Bonds, indemnity and surety. * * * *

Original Issue of Stock.

3. Capital stock, issue: On each original issue, whether on organization or reorganization, of certificates of stock, or of profits,

OR CONSOLIDATIONS

or of interest in property or accumulations, by any corporation, on each \$100 of face value or fraction thereof, 5 cents: Provided, That where a certificate is issued without face value, the tax shall be 5 cents per share, unless the actual value is in excess of \$100 per share, in which case the tax shall be 5 cents on each \$100 of actual value or fraction thereof.

The stamps representing the tax imposed by this subdivision shall be attached to the stock books and not to the certificates issued.

(Regulations 40, Revised to March 15, 1921.)

Article 33. "Reorganization" defined for Purposes of Stamp Regulations.

(1) (c) The term "reorganization" includes those business arrangements whereby the stock and bonds of a corporation are readjusted as to amount, income, or priority, or the property is sold to a new corporation for new stock and bonds, or is sold by the foreclosure of a mortgage upon it to a purchaser who buys for himself and his associates, and the various proceedings and transactions by which succession of corporations is brought about, and also the proceedings by which existing corporations are continued under a different organization without the creation of a new corporation. (As amended by T. D. 3118, Jan. 15, 1921.)

Article 4. Issues subject to tax.

(1) The issue of a greater number of shares of no par value stock in lieu of a smaller issue of such shares, previously made, without any change in the amount of the capital assets of the issuing corporation, is subject to stamp tax in the amount of the difference between the tax computed upon such issue and the tax computed upon the issue which it replaces. (Added by T. D. 3118, Jan. 15, 1921.)

(h) The issue of certificates of stock upon reorganization by a corporation is subject to tax.

(i) The issue of stock by a consolidated corporation in exchange for stock of the consolidating corporations is subject to tax.

(j) The issue of stock, in addition to its already existing stock, by the continuing corporation in case of a merger of corporations, is subject to tax.

Article 5. Issues not subject to tax.

(f) The issue, upon a merger of corporations, of certificates of stock of the same kind in substitution for the old certificates of stock is not subject to tax.

(i) The issue by a corporation of certificates of preferred stock in lieu of outstanding certificates of common stock, or vice versa, or the issue of certificates of preferred stock of one kind in lieu of certificates of preferred stock of another kind, without other considera-

REORGANIZATIONS, MERGERS

tion and without change in the amount of the authorized capital stock of the corporation, is not subject to tax. (As amended by T. D. 3118, Jan. 15, 1921.)

(The following is a digest of an opinion by the Solicitor of the Bureau of Internal Revenue.)

"Original issue, whether on organization or reorganization", construed.—The question is raised as to what constitutes an original issue of certificates of stock for the purpose of the stamp tax imposed upon the issue of capital stock.

The M Corporation was incorporated in the year 1916 with an authorized capital stock of \$7,000,000 divided as follows: First preferred stock \$1,000,000, second preferred stock \$1,500,000, common stock \$4,500,000, the certificates issued showed the authorized capitalization, and the stamp tax upon the stock issued was duly paid in accordance with the provisions of the Emergency War Revenue Act of October 22, 1914. On March 10, 1920, the charter of the corporation was amended to reduce the authorized capital stock to \$5,250,000, divided as follows: Preferred stock \$1,500,000, common stock \$3,750,000, and new certificates were prepared showing the changed capitalization. At this time all of the first preferred stock had been retired, and there was outstanding of the original issue \$4,500,000, made up as follows: Second preferred stock \$1,500,000, common stock \$3,000,000. The outstanding second preferred stock was noncumulative and bore 6 per cent interest and had a par value of \$50 per share. The outstanding common stock also had a par value of \$50 per share. The new preferred stock was 8 per cent cumulative stock and had a par value of \$100 per share, and the new common stock was of a par value of \$100 per share. The new preferred stock was exchanged for the outstanding second preferred stock at the ratio of 1 share for 2, and the new common stock was exchanged for the old at the same ratio. It is contended that under the decision of the Circuit Court of Appeals, Second Circuit, in the case of *Edwards v. Wabash Railway Company* (T. D. 3002) and T.D. 3014 no additional stamp tax was due by reason of this exchange.

In the *Wabash* case 5 per cent profit-sharing preferred stock A and common stock were exchanged for 5 per cent convertible preferred stock B in accordance with a provision contained in the original charter. All of the stock was par-value stock, the entire authorized issue of capital stock had been tax-paid at the time of the original issue, and the total authorized capitalization was not affected by the exchange. Upon these facts the court held:

In the case at bar when the plaintiff paid at the time of its organization the tax of 5 cents for each hundred dollars of face value of its total capital stock, including the A stock, the B stock, and the common stock, such payment was made once for all and constituted the payment of the tax on each original issue of the certificates of stock whenever and to whomsoever delivered. Whenever thereafter the plaintiff delivered the first certificates of the B stock it was not under obligation to pay again the tax on the B certificates. That had been already

OR CONSOLIDATIONS

done. And when subsequently the plaintiff exchanged the certificates of the B stock for certificates of the A stock and of the common stock it was not bound to pay again the tax on the certificates. That tax, too, had been already paid. The exchange of stock was an exchange of original certificates of one kind of stock for original certificates of two other kinds of stock, the tax on all of which had been previously paid.

In the instant case the total authorized capitalization of the corporation was changed and each share of the new stock, whether common or preferred, represented a fractional interest in a different capital stock. A new series of certificates was issued showing the change in the authorized capitalization and substituted for the outstanding certificates of the former corporation. The new preferred stock was cumulative convertible stock bearing 8 per cent interest; the stock for which it was substituted was noncumulative convertible stock bearing 6 per cent interest; and the common stock in the reorganized corporation was issued subject to these different charges. Under the circumstances, it is clear that the new stock issued was stock which had never been before issued and was under an authorization not theretofore existing but which arose out of the amendment of charter.

It is therefore believed that the issue of stock in question constituted an original issue on reorganization within the meaning of subdivision 3, Schedule A, Title XI, of the Revenue Act of 1918, and is subject to the tax imposed by that subdivision, and it is so held.

(Opinion of the *Solicitor of Internal Revenue*, by Carl A. Mapes, for the Solicitor. (Sol. Op. 71: 1-21).)

(*Revenue Act of 1918.*)

(Schedule A.—Stamp Taxes.)

Sales or Transfers of Stock.

4. Capital stock, sales or transfers: On all sales, or agreements to sell, or memoranda of sales or deliveries of, or transfers of legal title to shares of certificates of stock or of profits or of interest in property or accumulations in any corporation or to rights to subscribe for or to receive such shares or certificates, whether made upon or shown by the books of the corporation, or by any assignment in blank, or by any delivery, or by any paper or agreement or memorandum or other evidence of transfer or sale, whether entitling the holder in any manner to the benefit of such stock, interest, or rights, or not, on each \$100 of face value or fraction thereof, 2 cents, and where such shares are without par or face value, the tax shall be 2 cents on the transfer or sale or agreement to sell on each share, unless the actual value thereof is in excess of \$100 per share, in which case the tax shall be 2 cents on each \$100 of actual value or fraction thereof:

Provided, That it is not intended by this title to impose a tax upon an agreement evidencing a deposit of certificates as collateral

REORGANIZATIONS, MERGERS

security for money loaned thereon, which certificates are not actually sold, nor upon the delivery or transfer for such purpose of certificates so deposited:

Provided further, That the tax shall not be imposed upon deliveries or transfers to a broker for sale, nor upon deliveries or transfers by a broker to a customer for whom and upon whose order he has purchased same, but such deliveries or transfer shall be accompanied by a certificate setting forth the facts:

Provided further, That in case of sale where the evidence of transfer is shown only by the books of the corporation the stamp shall be placed upon such books; and where the change of ownership is by transfer of the certificate the stamp shall be placed upon the certificate; and in cases of an agreement to sell or where the transfer is by delivery of the certificate assigned in blank there shall be made and delivered by the seller to the buyer a bill or memorandum of such sale, to which the stamp shall be affixed; and every bill or memorandum of sale or agreement to sell before mentioned shall show the date thereof, the name of the seller, the amount of the sale, and the matter or thing to which it refers.

Any person liable to pay the tax as herein provided, or anyone who acts in the matter as agent or broker for such person, who makes any such sale, or who in pursuance of any such sale delivers any certificate or evidence of the sale of any stock, interest or right, or bill or memorandum thereof, as herein required, without having the proper stamps affixed thereto with intent to evade the foregoing provisions, shall be deemed guilty of a misdemeanor, and upon conviction thereof shall pay a fine of not exceeding \$1,000, or be imprisoned not more than six months, or both.

(Regulations No 40, Revised, as amended to March 15, 1921.)

Article 12. Sales and Transfers Subject to Tax.

(j) The transfer or surrender of stock to a corporation, for the purposes of the corporation, whether or not it intends eventually to sell such stock, is subject to tax.

(t) The transfer of stock of a corporation to be merged to the merging corporation prior to the actual merging and as a condition precedent to the merger is subject to tax.

Article 13. Sales and Transfers not Subject to Tax.

(d) The surrender of the stock of the consolidating corporation in exchange for stock in the consolidated corporation, in the case of consolidation of two or more corporations, is not subject to tax.

(e) The transfer of the stock of a merged corporation in exchange for stock of the merging corporation at the time and as a part of a statutory merger is not subject to tax, nor is the substitution of new certificates for the certificates representing the old stock of the merging corporation.

OR CONSOLIDATIONS

(*Revenue Act of 1918.*)

[Schedule A.—Stamp Taxes.]

Conveyances.

7. Conveyances: Deed, instrument, or writing, whereby any lands, tenements, or other realty sold shall be granted, assigned, transferred, or otherwise conveyed to, or vested in, the purchaser or purchasers, or any other person or persons, by his, her, or their direction, when the consideration or value of the interest or property conveyed, exclusive of the value of any lien or encumbrance remaining thereon at the time of sale, exceeds \$100 and does not exceed \$500, 50 cents; and for each additional \$500 or fractional part thereof, 50 cents. This subdivision shall not apply to any instrument or writing given to secure a debt.

(*Regulations 55, Revised, as amended to March 15, 1921, and available special rulings.*)

Art. 70. "Sold" defined.—The term "sold" imports the transfer of the absolute or general title for a valuable consideration or price.

Art. 81. Stock in corporation a valuable consideration.—Stock in a corporation is a valuable consideration for the transfer of real property.

Art. 103. Conveyance by corporation to owner of all the capital stock.—A conveyance of real estate by a corporation without valuable consideration to an owner of all its capital stock in consequence of its dissolution is not subject to tax.

Stamp tax liability on account of original issue and transfer of stock and conveyance of real property incident to the reorganization of a corporation under the laws of another State, without more.—Reference is made to your letter of February 5, 1920, in which you inquire as to the application of stamp tax in the case where the Co. of Illinois has been reorganized into the [same name] Co. under the laws of the State of Ohio. [See note below.] You are advised that where a company gives up its articles of incorporation in the State of Illinois and is incorporated in the State of Ohio, the application of stamp tax is to be determined by the method followed. In any event stamp tax on original issue applies to the stock to be issued by the new corporation. The transfer of stock among the assets of the old corporation to the new corporation is subject to stamp tax. Conveyance of real property from the old corporation to the new corporation in consideration of the issue of new stock to the old corporation or to its stockholders is subject to stamp tax on the basis of the value of the property. If the new stock is issued to the old corporation the transfer of that stock from the old

REORGANIZATIONS, MERGERS

corporation to its stockholders is subject to stamp tax. If the new stock is issued to the stockholders of the old corporation the transfer of the right to receive that stock from the old corporation is subject to transfer stamp tax additional to the original issue stamp tax. If the old stock is surrendered to the old corporation for extinguishment no transfer stamp tax accrues. If the old stock is surrendered to the new corporation and constitutes it a corporate stockholder that surrender is taxable. (Letter to The Corporation Trust Company, signed by Commissioner Daniel C. Roper, and dated February 26, 1920.)

[Note.—The facts submitted with names omitted, on which the above ruling is based, are as follows:

The Co. was organized many years ago under the laws of Illinois. A new corporation of the same name has been organized under the laws of Ohio and will acquire the property and continue the business of the Illinois corporation.

The Ohio corporation will take over all assets (both real and personal) and assume all liabilities of the Illinois corporation. In payment for the property, the Ohio corporation will deliver to the Illinois corporation certificates of stock issued in the names of the present stockholders and for the number of shares owned by them, respectively, in the Illinois corporation. The Illinois corporation will receive from its stockholders its own shares of stock, in exchange for a like number of shares of the Ohio corporation, and will then be dissolved.

The identical property will remain in the possession of the identical stockholders and the proportionate interest of each stockholder will remain unchanged, the sole purpose of the transaction being merely to domicile the present enterprise in Ohio as a matter of convenience.]

WHAT THE CORPORATION TRUST COMPANY AND AFFILIATED COMPANIES DO

That attorneys may know to what extent they can call upon us for assistance, an outline is given of the departments maintained, and services rendered, by The Corporation Trust Company System.

Domestic Corporation Department.

Drafts for approval and assistance of attorneys only, the papers incidental to the organization, and attends to the filing of them for the incorporation of companies in any state, territory or possession of the United States and in Canada or England. Subsequent to organization, maintains the office required by statute and furnishes office, resident agent, officer or director necessary to keep the

corporation in good standing and to avoid a possible forfeiture of the charter. Gives the attorney notice of every state report which must be filed and tax which must be paid. Delivers to attorney all papers served upon the resident office, agent, officer or director, giving telegraphic advice when necessary.

Foreign Corporation Department.

Drafts for approval and submits to attorneys only papers for qualification, and attends to the filing of all documents required to enable a corporation to obtain permission to transact business in any state, territory or possession of the United States, and in Canada or England. Furnishes the agent, statutory office or other representation required in order to comply with the particular state statute and avoid the forfeiture of the right to do business. Notifies the attorney of all state reports that must be filed and taxes that must be paid to keep the license valid. Forwards to the attorney all reports, tax blanks, process or other documents which may be served upon the local agent, giving telegraphic advice when necessary.

Report and Tax Department.

Maintained for the purpose of notifying attorneys of every state report which must be made and tax which must be paid to keep the corporation, either as a domestic or foreign corporation, in good standing. This service is for the benefit of those attorneys whose clients furnish their own office, agent or other statutory representation.

Transfer Department.

Maintains in New York, Jersey City, Chicago and Philadelphia, thoroughly equipped departments for the transfer and registration of stock and other corporate securities. A special pamphlet covering this service will be sent to anyone interested.

Legislative Department.

Furnishes prompt and accurate reports on all subjects of legislation introduced or enacted in Congress and of the daily action thereon. Furnishes copies of bills as introduced, amended and enacted into law.

Federal Department.

Maintains an office in Washington for the purpose of assisting attorneys in obtaining information and copies of documents from

any of the departments. Furnishes agent for common carriers to accept service of orders, process, etc., of the Interstate Commerce Commission.

Income Tax Service.

Reports all rulings or regulations under the Federal Income Tax Law.

War Tax Service.

Reports rulings and regulations of the Federal Estate Tax, the Capital Stock Tax, the Excess Profits Tax, the Sales and Semi-Luxury Taxes, and other Special and Miscellaneous Taxes of the General Revenue Law.

New York Income Tax Service.

Is an indexed compilation of the Personal Income Tax and Corporation Income Tax and all formal regulations now in force. Many informal rulings on perplexing points, court decisions, in a loose leaf binder kept always up-to-date by means of sequentially numbered printed pages sent to the subscriber under first class postage.

Federal Trade Commission Service.

Reports rulings and regulations of the Federal Trade Commission.

Federal Reserve Act Service.

Reports rulings and regulations of the Federal Reserve Board.

Supreme Court Service.

Reports decisions of the United States Supreme Court.

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